



INDONESIA: ECONOMIC AND FINANCIAL HIGHLIGHTS MAY 2006

Summary:

- On May 31, the Central Bureau of Statistics (BPS) announced a slight increase in consumer price inflation, at 15.6 year-on-year (YoY) and 0.4% month-on-month (MoM).
- BPS also announced on May 15 first quarter GDP growth of 4.6% YoY, the slowest pace in two years.
- On May 9, Bank Indonesia (BI) cut its benchmark rate by a quarter point to 12.5%, after five months at 12.75%, and maintained it at that level at its June 6 monetary policy board meeting.
- The Jakarta Stock Exchange (JSX) Composite Index fell by 15.2% from May 15 - June 8 in line with volatility in other emerging markets.
- After strong appreciation in the first quarter, the rupiah experienced significant volatility against the USD beginning in mid-May, hitting a four-month low of 9,420/USD on May 16. The rupiah closed at Rp 9,395/USD on June 8.
- Moody's Rating Service upgraded Indonesia's sovereign bond rating from B2 to B1 on May 19. Also on May 19, Moody's raised the ratings of the constrained foreign currency debts and deposits of nine Indonesian banks to "stable."
- On May 29, the Government of Indonesia (GOI) said it would repay its USD 7.8 billion standby reserves loan to the International Monetary Fund (IMF) three years ahead of schedule.
- On May 30, Indonesia's largest lender, state-owned Bank Mandiri, reported a 1.8% decline in its after tax profit in Q1 2006, partly due to high interest costs.
- On May 30, Indonesia's third largest state-owned bank, Bank Rakyat Indonesia (BRI), announced a plan to write-off loans to earthquake victims in Yogyakarta.
- This report uses an exchange rate of Rp 9,220 per 1 USD.

Inflation Rises Slightly in May

On May 31, BPS announced that the Consumer Price Index (CPI) rose 15.6% YoY, and 0.4% MoM in May 2006. Higher clothing prices, surprisingly, were a main driver of the increase. Core inflation also increased slightly to 9.5% (YoY) from 9.4% in the previous month.

CPI Components

Components	MoM	YoY
Food stuff	0.3	16.5
Food, beverages, tobacco, cigarettes	0.3	12.8
Housing, water, electricity, oil/gas	0.3	12.8
Clothing	2.0	10.3
Health	0.6	7.3
Education, recreation, and sport	0.1	8.0
Transportation, communication, financial services	0.2	30.9
TOTAL	0.4	15.6

Source: Central Bureau of Statistics (BPS)

Q1 GDP Growth Slows and Unemployment Rises

On May 15, BPS announced that GDP growth in the first quarter of 2006 slowed to 4.6% YoY, the weakest quarterly YoY growth rate in almost two years. In comparison, real GDP grew 4.9% in Q4 2005. Government expenditures did not rise as much as expected, increasing only by 14.1% YoY after expanding 29.8% Q4 2005. Coordinating Minister for the Economy Boediono admitted that the GOI had failed to accelerate spending in the first four months of the year due to regional and central government bureaucratic delays. A Ministry of Finance budget realization data for Q1 2006 showed the GOI had only spent about Rp 3.5 trillion (USD 380 million) of a budgeted Rp 62.9 trillion (USD 6.8 billion) in capital expenditures during the first quarter, and about Rp 4.2 trillion (USD 455.5 million) of a budgeted Rp 36.9 trillion (USD 4 billion) in social spending. Realized transfers to regions were much closer to their budgeted levels at Rp 49.3 trillion (USD 5.3 billion), or 22.4% of the full year Rp 220.1 trillion (USD 23.9 billion) target.

Private consumption growth also slowed to 3.2%, compared with 4.2% in the previous quarter, with analysts citing high consumer interest rates and higher fuel prices as the culprits. Retail sales in the auto sector, for example, plunged by nearly 45% year-on year to below 80,000 units in the first quarter. "People are still feeling the impact of the fuel price increase last year, and high interest rates have prevented a pickup in economic growth", said Bank Danamon President Director Sebastian Paredes. Exports, however, rose a robust 10.8% YoY in Q1 2006 versus 7.4% in Q4 2005. Investment growth increased slightly to 2.9% on a YoY basis, boosted by strong inflows of foreign direct investment (FDI).

On June 1, BPS also reported that the Indonesian workforce reached 106.3 million in February 2006, an increase of 500,000 YoY. The unemployment rate as of February 2006 was 10.4, slightly higher than the February 2005 level of 10.3%. Only about 40-50% of Indonesia's workforce is in the formal sector.

Indonesian YoY Real GDP Growth:

A. By Production Category	% Change Q1-06 vs Q1-05	% Change Q4-05 vs Q4-04	Share of GDP
Manufacturing	2.0	2.9	28.7
Agriculture	3.9	5.5	13.4
Retail, Hotel, Restaurant	4.2	6.0	15.0
Mining	7.0	1.9	10.5
Services	5.4	6.0	9.8
Finance and Leasing	5.1	5.2	8.3
Construction	7.2	6.9	6.4
Transportation and Communication	11.0	10.8	7.0
Electricity, Gas, Water	5.2	6.1	0.9
TOTAL (categories weighted)	4.6	4.9	100.0

B. By Expenditure Category	% Change Q1-06 vs Q1-05	% Change Q4-05 vs Q4-04	Share of GDP
Private Consumption	3.2	4.2	58.9
Government Expenditure	14.2	30.0	6.9
Investment	2.9	1.8	21.6
Exports	10.8	7.4	42.8
Imports	5.1	3.7	34.8

Source: Central Bureau of Statistics (BPS)

Bank Indonesia Cuts Interest Rate to 12.5%

BI cut its benchmark interest rate on May 9 to 12.5%, after holding rates steady at 12.75% since December 6, 2005. At its June 6 board meeting, BI maintained the interest rate at that level. In a June 6 statement, BI Governor Burhanuddin Abdullah noted significant outflows of foreign capital in May created some pressure on the rupiah and pass-through inflation, but said inflation numbers and banking indicators are still manageable.

Stock Market and Rupiah Volatility

In line with stock markets in other emerging markets, the Jakarta Stock Exchange (JSX) Composite Index underwent a major correction in the second half of May, shedding more than USD 10 billion in market value. The sell-off continued through June 8, with the JSX composite index closing at 1241.3, a decrease of 15.2% since May 15. The President Director of the JSX said on May 23 that unlike some exchanges, JSX does not have authority to temporarily suspend trading in case of excess volatility, but must request permission from the Capital Markets Supervisory Authority (BAPEPAM). The JSX composite index had risen more than 14% from January 1 to May 15, 2006.

After strong appreciation in the first quarter, the rupiah also came under pressure in the second half of May when volatility struck many emerging markets. The rupiah hit a four-

month low of Rp 9,420/USD on May 16, recovered to Rp 9,220/USD by the end of May, but again came under pressure in early June, closing at Rp 9,395/USD on June 8. BI Governor Burhanuddin Adbullah told the media he saw "no fundamental reasons" behind the rupiah's depreciation, and said BI would "continue to guard the rupiah and to be in the market," according to Dow Jones Newswires.

Moody's Upgrades Sovereign Ratings for Indonesia

On May 19, Moody's Investor Service upgraded Indonesia's foreign currency country ceiling for bonds and the foreign- and domestic-currency government bond ratings to "B1" from "B2", citing improved fiscal health (Moody's B1 rating is four notches below investment grade.) Moody's also upgraded the foreign currency country ceiling for bank deposits to "B2" from "B3", while the local currency bank deposit ceiling and the local currency guideline remained unchanged at "Baa2". Moody's said further upgrades would depend on the maintenance of sound government finances, improvements in the investment climate, and increased foreign direct investment. Standard and Poor's Ratings Services rates Indonesia's sovereign credit four notches below investment grade, while Fitch rates Indonesia's sovereign debt three notches below investment grade.

Bank Rating Upgrades

Also on May 19, Moody's announced it had raised the ratings of the constrained foreign currency debts and deposits of nine Indonesian banks. The revised ratings carry a "stable" outlook. According to Moody's, the increase in the subordinated debt ratings of state-owned banks reflects the government's enhanced ability to support the banking system given its increased resources. Non-prime short-term deposit and bank financial strength ratings of all the nine banks were unaffected. On May 23 Fitch also upgraded national ratings for eight Indonesian banks and support ratings for two banks, Buana and NISP.

Indonesian Bank Ratings Upgrades

Bank/Rating	Agency	Previous	Upgrade
Mandiri			
Subordinated debt	Moody's	B2/B3	B1/B1
Long-term deposit	Moody's	B3	B2
National long-term	Fitch	A	AA
BNI			
Subordinated debt	Moody's	B2/B3	B1/B1
Long-term deposit	Moody's	B3	B2
National long-term	Fitch	BBB+	A+
BCA			
National long-term	Fitch	A-	AA
BRI			
Subordinated debt	Moody's	B3	B1
Long-term deposit	Moody's	B3	B2
National long-term	Fitch	A+	AA+
BTN			
Long-term deposit	Moody's	B3	B2
Danamon			
Subordinated debt	Moody's	B2	B1
National long-term	Fitch	A-	AA-
BII			
Subordinated debt	Moody's	B2	B1
Long-term deposit	Moody's	B3	B2
National long-term	Fitch	BBB+	AA-
Niaga			
Subordinated debt	Moody's	B2	B1
Long-term deposit	Moody's	B3	B2
Permata			
Long-term deposit	Moody's	B3	B2
Panin			
Long-term deposit	Moody's	B3	B2
NISP			
National long-term	Fitch	A-	AA+
Support	Fitch	4	3
Buana			
National long-term	Fitch	A-	AA+
Support	Fitch	4	3

Source: XFN-Asia, Fitch Ratings

Bank Mandiri Q1 Loss, New Directors

On May 30, Indonesia's largest state-owned bank, Bank Mandiri, reported a 1.8% decline in first-quarter after-tax profit to Rp 510 billion (USD 55.3 million). The bank's profits declined partly due to high interest costs. Total assets of the bank rose 2.2% YoY to Rp 254.9 trillion (USD 27.6 billion), while total loans expanded 5.6% to Rp 105.1 trillion

(USD 11.4 billion). Mandiri's net non-performing loan ratio (NPL) fell to 15.8% in the first quarter from 16% at the end of December, while its gross NPLs increased to 27.7% from 26%. The bank said it aims to reduce its net NPL ratio to 5% by the end of 2007. Shareholders also approved distribution of 50% dividend, or Rp 302 billion (USD 32.8 million) of 2005 net profit

On May 23, Mandiri shareholders ratified the appointment of five new directors and the removal of Finance Director J.B. Kendarto. The shareholders also approved the appointment of President Commissioner Edwin Gerungan to the additional role of Independent Commissioner. Mandiri's Board of Directors now has eleven members, while the Board of Commissioners has seven. Mandiri President Director Agus Martowardojo said that the expansion was needed to improve performance.

Indonesia Says It Will Repay IMF Early

Indonesian President Susilo Bambang Yudhoyono (SBY) announced on May 23 that Indonesia would repay the USD 7.7 billion remaining of its standby reserve loan with the International Monetary Fund (IMF) in two tranches, one each in 2006 and 2007. Yudhoyono emphasized that early repayment to IMF is important to increase the GOI's credibility and improve market confidence. While many analysts believe Indonesia can easily afford the repayment -- FX reserves were USD 44.2 billion as of May 29 -- some have questioned the timing given the recent bout of emerging market volatility. The GOI did not immediately announce a schedule for the repayments, but said the first could come as early as June.

BRI Writes Off Loans for Earthquake Victims

Indonesia's third largest bank, the state-owned Bank Rakyat Indonesia (BRI) announced on May 30 that it would write-off Rp 140 billion (USD 15.2 million) in loans for its earthquake affected customers in Yogyakarta. BRI's total loans to the region are Rp 339 billion (USD 36.8 million), or 0.95% of total loans nationwide. "With the write-off, potential loss from interest payment is Rp 30 billion (USD 3.3 million)," BRI's President Director Sofyan Basir told the press. BRI budgeted RP 265 billion (USD 28.7 million) for disaster write-offs in 2006.

Selected Economic, Monetary & Financial Statistics

	Feb 06	Mar 06	Apr 06	May 06
CPI Inflation (YoY)	17.92	15.74	15.4	15.60
CPI Inflation (MoM)	0.58	0.03	0.05	0.37
Rp/USD Exchange rate ¹	9,185	9,075	8,775	9,220
30-day SBI Interest Rate ²	12.74	12.73	12.75	12.50
Foreign reserves ³	35.5	40.1	42.8	44.2
JSX Composite Index	1230.7	1323.0	1464.4	1330.0
Exports (USD billion)	7.35	7.45	7.6	
% Change (YoY)	15.18	2.76	11.9	

Import (USD billion)	4.51	4.35	4.8	
% Change (YoY)	4.47	-12.65	-3.7	
Trade Balance ⁵	2.84	3.10	2.8	

Source: Bank Indonesia, BPS

(1) Rp/USD, end of period

(2) End of period

(3) USD billions, end of period

(4) Jakarta Stock Exchange average daily transaction volume, in billions of shares

(5) USD billions

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